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The Not So Slippery Slope: The Eighth Circuit Determines That Employer-Paid Airfare Is Not Wages Subject to Withholding Taxes

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THE NOT SO SLIPPERY SLOPE: THE EIGHTH CIRCUIT DETERMINES THAT EMPLOYER-PAID AIRFARE IS NOT "WAGES" SUBJECT TO WITHHOLDING TAXES

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"Home may be where the heart is, but it definitely is not at Dead Horse at Prudhoe Bay on the North Slope of Alaska."[1] Indeed, whether [the town of] Dead Horse could constitute a "tax home" lay at the very heart of a recent Eighth Circuit Court of Appeals decision, *HB & R, Inc. v. United States*.[2] Set against a backdrop of contention concerning the location of an employee's tax home and its impact on employment related travel expenses, the Eighth Circuit determined that employer-paid airfare did not constitute "wages" subject to withholding taxes.[3] To understand the Eighth Circuit's analysis, however, it is necessary to consider certain basic tax issues relevant to employee travel.

I. LEGAL BACKGROUND

A. THE WITHHOLDING OBLIGATION

"The employment relationship involves two distinct taxpayers: the employer and the employee."[4] Compensation in the form of wages constitutes gross income subject to taxation for the employee.[5] Compensation in the form of "fringe benefits" that are not de minimis also constitutes gross income subject to taxation for the employee.[6] Thus, what an employer pays in wages and fringe benefits is taxable income to the employee and an ordinary and necessary business deduction to the employer.[7]

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1. HB & R, Inc. v. United States, No. A1-96-141, slip op. at 1 (D. N.D. Apr. 28, 1998).

2. 229 F.3d 688 (8th Cir. 2000).

3. *HB & R*, 229 F.3d at 690.

4. *Id.*

5. *See* 26 U.S.C. § 61(a)(1) (1994) (defining gross income as encompassing "all income from whatever source derived," including "[c]ompensation for services, including fees, commissions, fringe benefits, and similar items") [hereinafter I.R.C.].

6. *Id.* Most examples of taxable fringe benefits include benefits with an element of personal pleasure or recreation, such as employer-provided tickets to sporting events, country club memberships, or airline tickets for vacation destinations. *See* 26 C.F.R. § 1.61-21(a)(1) (2001). Likewise, the fringe benefit of commuting to work in an employer-provided vehicle is valued at $1.50 per each one-way commute. *Id.* § 1.61-21(k)(3).

7. *See* I.R.C. § 61(a) (defining gross income); I.R.C. § 162(a) (1994 & Supp. V 1999) (providing

Because wages constitute taxable income to the employee, the employee owes federal income tax on the wages.[8] In addition, both the employer and the employee owe Federal Insurance Contribution Act (FICA) taxes, such as Medicare and social security, on the wages.[9] To make the tax collection system more efficient by collecting taxes "at the source," employers are required to deduct and withhold from an employee's wages the federal income taxes and FICA taxes that the employee is likely to owe.[10] Employers then remit to the government these withheld sums, along with the employer's own share of the FICA tax.[11]

The employer's obligation to withhold extends only to an employee's wages.[12] It does not apply to other types of employee income, such as dividends or the reimbursement of deductible expenses.[13] While wages usually constitute income, many items that qualify as income are clearly not wages.[14] Thus, discerning between the two for withholding purposes is imperative. When a tax deficiency is assessed based upon an employer's alleged failure to withhold, the definition of "wages" in the withholding statutes becomes critical.

B. THE DEFINITION OF "WAGES"

Under Internal Revenue Code § 3401(a), "wages" for income tax withholding purposes include "all remuneration [for employment], including the cash value of all remuneration (including benefits) paid in any medium other than cash."[15] Similarly, "wages" for FICA tax withholding purposes include "all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any

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that a business may deduct ordinary and necessary expenses incurred in the pursuit of business).

8. *See* I.R.C. § 1 (1994 & Supp. V 1999) (setting forth the tax imposed).

9. *See* I.R.C. § 3101 (1994) (setting forth the employee tax); I.R.C. § 3111 (1994) (setting forth the employer tax). The FICA tax rules are codified in chapter 21 of the Code. I.R.C. §§ 3101-3121 (1994 & Supp. V 1999). Currently, § 3101 imposes an aggregate tax of 7.65% on an individual's wages, payable by the employee to the federal government. Similarly, § 3111 imposes an aggregate tax of 7.65% on an individual's wages, payable by the employer to the federal government.

10. *See* I.R.C. § 3402(a) (1994) (setting forth the withholding of income tax requirement); I.R.C. § 3102(a) (1994) (setting forth the withholding of FICA tax requirement). The amount of tax to be withheld and paid is determined by the amount of "wages" paid to the employee. I.R.C. §§ 3111(a), 3121(a), 3401(a) (1994 & Supp. V 1999).

11. *See* I.R.C. §§ 3102, 3402 (1994).

12. *Id.* §§ 3102, 3402(a).

13. Section 3101 imposes the employee FICA tax only on wages received by the individual with respect to employment, as that term is defined in § 3121(b). Section 3111 imposes the employer FICA tax only on wages paid to an individual with respect to employment, as that term is defined in § 3121(b). In turn, § 3121(b) defines "employment" as "any service, of whatever nature, performed" by an employee. Thus, to be subject to FICA taxation, the amounts received by the employee must be (1) income (for the employee's portion); (2) wages (as defined in § 3121(b)); and (3) received with respect to employment. *Kevin Wiggins, Capital Gain v. Ordinary Income and the FICA Tax Treatment of Employee Stock Purchase Plans*, THE TAX LAWYER, Spring 2000, at 5.

14. Cent. Ill. Pub. Serv. Co. v. Unites States, 435 U.S. 21, 25 (1918).

15. I.R.C. § 3401(a).

medium other than cash."[16] Accordingly, for both income and FICA tax withholding purposes, the Code defines "wages" as including all non-cash remuneration or fringe benefits valued at the excess of its fair market value over any amount paid by the employee for the benefit.[17] Under both statutes, however, "wages" do not include amounts that the employer reasonably believes are excludable from the employee's income under Code § 132.[18]

Code § 132 permits an employee to exclude from income, among other items, any "working condition fringe" which, if paid for by the employee, would be deductible under Code § 162 as an employee business expense.[19] Section 162, in turn, provides for the deduction of ordinary and necessary trade or business expenses, including travel expenses incurred "while away from home in the pursuit of a trade or business."[20] An employee may not, however, deduct personal expenses.[21] Thus, to the extent that any travel expenses are predominantly personal in nature, they are not deductible under § 162.[22] In aggregate, the FICA and income tax withholding statutes provide that if the costs associated with work-related travel would have been

16. I.R.C. § 3121(a).

17. I.R.C. § 132 (1994 & Supp. V 1999); *see also* Finance Comm. Portion of Reconciliation Report at 367-68, *reprinted in* 1986 U.S.C.C.A.N. 326 (discussing application of employment taxes to the value of free airfare provided by airlines to their employees).

18. I.R.C. §§ 3121(a)(20), 3401(a)(9) (1994 & Supp. V 1999). Specifically, Code § 3121(a)(20) excludes from wages "any benefit provided to or on behalf of an employee if at the time such benefit is provided it is reasonable to believe that the employee will be able to exclude such benefit from income under section . . . 132." Likewise, Code § 3401(a)(19) excludes from wages "any benefit provided to or on behalf of an employee if at the time such benefit is provided it is reasonable to believe that the employee will be able to exclude such benefit from income under section . . . 132." Exempting from withholding those amounts that do not constitute taxable income is consistent with the legislative history of the Social Security Act, 49 Stat. 620 (1935) (codified as amended at 42 U.S.C. §§ 301-306 (1994 & Supp. V 1999)). Specifically, with regard to the FICA taxation scheme, Senator Harrison remarked that the tax on employees would be a tax on their wages and that employers "would also pay a similar tax at the same rates, based on the *taxable pay* of each employee." 79 CONG. REC. 9268 (1935) (emphasis added).

19. I.R.C. § 132(d) defines a "working condition fringe" as "any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167." Also excludable under § 132(b) are "no-additional-cost" services and qualified employee discounts provided by an employer to an employee for use by the employee or the employee's spouse and dependent children. To be excluded under the "no-additional-cost" exception, the service must be the same type of service that is sold to the public in the ordinary course of the employer's line of business in which the employee performs services. *See* I.R.C. § 132(b); *see also* Finance Comm., *supra* note 17, at 367-68.

20. I.R.C. § 162(a)(2). The travel expense deduction specifically includes "amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances." *Id.*

21. I.R.C. § 262 (1994).

22. *See* I.R.C. § 262(a) (providing that "no deduction shall be allowed for personal, living, or family expenses"); *see also* Commissioner v. Flowers, 326 U.S. 465 (1945) (determining that an employee's travel expenses were incurred because of his personal choice to live far away from his employment and thus, were not deductible under § 162).

deductible to the employee if the employee paid for it, the costs are not "wages" subject to withholding if the employer pays for the travel.

C. EMPLOYEE'S DEDUCTION OF COMMUTING EXPENSES UNDER § 162

The deductibility of travel expenses under § 162 has been a contested issue since the section's inception.[23] In 1945, the United States Supreme Court made its most significant pronouncement on the issue in *Commissioner v. Flowers*.[24] The taxpayer in *Flowers* was general counsel for Gulf, Mobile & Ohio Railroad, which maintained its primary office in Mobile, Alabama.[25] For personal reasons however, Flowers resided in Jackson, Mississippi, and traveled to Mobile thirty-three times during 1939 and forty times during 1940 to perform his job duties.[26] Flowers personally paid for the travel expenses and then deducted the costs as ordinary and necessary business expenses under § 162.[27]

In analyzing whether Flowers' travel expenses were deductible, the Court formulated a three-pronged test for the deduction of travel expenses.[28] First, the expenses must be "reasonable and necessary traveling expense[s], as that term is generally understood," such as for transportation fares, food, and lodging.[29] Second, "[t]he expense must be incurred 'while away from home.'"[30] Third, "[t]he expense must be incurred in [the] pursuit of business."[31] The third prong is met when there is a direct connection between the expenditure and the carrying on of the employer's business.[32]

Concluding that Flowers' expenses were not deductible, the United States Supreme Court stated that whether Flowers was "away from home" was irrelevant since the expenses were not incurred in the pursuit of business, as required by the third prong of the deductibility test.[33]

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23. *See, e.g.*, Bixler v. Commissioner, 5 B.T.A. 1181 (1927). In *Bixler*, the Board of Tax Appeals held that the precursor to § 162(a)(2) was intended to permit a deduction for travel expenses only if the expenses were incurred while the taxpayer was away from his post of duty or place of employment. *Id.* at 1184.

24. 326 U.S. 465 (1945).

25. *Flowers*, 326 U.S. at 467.

26. *Id.* at 467-68. Flowers worked for the railroad in Mobile for a total of 66 days in 1939 and 102 days in 1940. *Id.* at 468.

27. *Id.* at 468-69.

28. *Id.* at 470.

29. *Id.*

30. *Id.*; *see also infra* Part I.D.

31. Commissioner v. Flowers, 326 U.S. 465, 470 (1945).

32. *Id.*

33. *Id.* at 471-72. After noting the conflicting definitions of "home," the Court stated, "[w]e deem it unnecessary here to enter into or to decide this conflict." *Id.* at 472.

With respect to the expenses in question, the Court specifically stated that:

> They were incurred solely as a result of the taxpayer's desire to maintain a home in Jackson while working in Mobile, a factor irrelevant to the maintenance and prosecution of the railroad's legal business. The railroad did not require him to travel on business from Jackson or Mobile or to maintain living quarters in both cities.
> . . . The exigencies of business rather than the personal conveniences and necessities of the traveler must be the motivating factors. Such was not the case here.[34]

Thus, *Flowers* is often cited for the general rule that an employee's expenses in commuting from home to work are personal expenses, not deductible business expenses, because the location of the employer's residence in relation to the employee's place of business is generally motivated by personal, rather than business, concerns.[35] Indeed, Treasury Regulation section 1.262-1(b)(5) expressly follows *Flowers* by providing that "[t]he taxpayer's costs of commuting to his place of business or employment are personal expenses and do not qualify as deductible expenses."[36] Thus, the central importance of *Flowers* is its requirement of a direct connection between the expenditure and the "exigencies" of the employer's business.[37] Under *Flowers*, if the exigencies of the employer's business motivate the employee's travel, the employee can deduct the travel expenses if the employer does not reimburse the employee.[38] Conversely, if the employee's travel is motivated by purely personal reasons, the employee cannot deduct travel expenses.[39]

Consequently, when an employer requires an employee to travel to a temporary work-site, courts have generally held that the employee can deduct the expenses of such travel since the costs are incurred because of the exigencies of the employer's business, rather than the personal desires of the employee.[40] By requiring that the taxpayer's travel costs

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34. *Id.* at 473-74.

35. *See, e.g.*, Sanders v. Commissioner, 439 F.2d 296, 297 (9th Cir. 1971).

36. 26 C.F.R. § 1.262-1(b)(5) (2001); *see also* 26 C.F.R. § 1.162-2(e) (2001) (providing that "[c]ommuters' fares are not considered as business expenses and are not deductible").

37. Commissioner v. Flowers, 326 U.S. 465, 473-74 (1945).

38. *Id.* at 474.

39. *Id.* at 473.

40. *Compare* Frederick v. Commissioner, 603 F.2d 1292, 1295-96 (8th Cir. 1979) (upholding a finding that a three-year stint at a distant construction project was "temporary" and concluding that the costs of travel to the distant site were deductible) *with* Walraven v. Commissioner, 815 F.2d 1246, 1248 (8th Cir. 1987) (finding that a construction worker's three-year work term at a nuclear power plant project 150 miles from his residence was not temporary and concluding that the costs of his travel to

be incurred in the pursuit of and because of the exigencies of his employer's business, *Flowers* has provided a useful mechanism for sorting between travel motivated by business reasons and travel motivated by personal reasons.[41] The Internal Revenue Service (the "Service") has apparently been dissatisfied with its ability to limit deductions under the third prong of *Flowers*. Thus, the Service has also attacked commuting expenses under the second prong of *Flowers*, which requires that the expenses be incurred while away from home, by manipulating the definition of "home" and when an employee has travel away from such home.[42]

D. THE DIVERGENCE IN THE MEANING OF "HOME"

In accordance with the second prong of *Flowers*, courts often have analyzed an employee's deduction of travel expenses based on whether the employee was "away from home."[43] The debate concerning what constitutes an employee's tax home for such purposes, however, has resulted in a split of authority.[44] Pursuant to that split, some courts have interpreted "home" to mean residential home, whereas others have interpreted "home" to mean the place where the employee works.[45] The Supreme Court, despite three opportunities to resolve the split in authority, has not provided any definitive guidance to the circuit courts.[46] For

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the work-site were not deductible). *See generally* Michael D. Rose, *The Deductibility of Daily Transportation Expenses To and From Distant Work Sites*, 36 VAND. L. REV. 541 (1983). Most courts continued to analyze the deductibility of travel expenses based on whether the employee was traveling to a permanent or temporary work-site. *See, e.g.*, Harris v. Commissioner, 39 T.C.M. (CCH) 1126, 1132 (1980), *aff'd* 679 F.2d 898 (9th Cir. 1982); McCallister v. Commissioner, 70 T.C. 505, 506 (1978); Norwood v. Commissioner, 66 T.C. 467 (1976). The Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 (codified at 42 U.S.C. §§ 13201-13556 (1994 & Supp. V 1999)) clarified the issue of what constitutes a temporary work-site for deduction of travel expenses. As a result of the Energy Policy Act of 1992, § 162(a) was amended to provide that a "taxpayer shall not be treated as being temporarily away from home during any period of employment if such period exceeds 1 year."

41. *Flowers*, 326 U.S. at 474.

42. According to the Commissioner, "away from home" means away from the taxpayer's "tax home," and a taxpayer's "tax home" is that person's "home post" or place of employment. *Flowers*, 326 U.S. at 471. This analysis was adopted by a number of courts, yet rejected by others. *Compare* O'Toole v. Commissioner, 243 F.2d 302, 303 (2d Cir. 1957) (stating that "home" means a "taxpayer's principal place of business or employment") *and* Barnhill v. Commissioner, 148 F.2d 913, 917 (4th Cir. 1945) *with* Steinhort v. Commissioner, 335 F.2d 496, 503 (5th Cir. 1964) *and* Wright v. Hartsell, 305 F.2d 221, 224 (9th Cir. 1962) (rejecting the Service's argument that "home" means principal place of business). As a result of those cases adopting the "tax home" concept, the word "home" became a term of art with a meaning different from its normal usage as a residence, domicile, or dwelling place. *See, e.g., O'Toole*, 243 F.2d at 303 (stating taxpayer's home was where he was employed).

43. *See, e.g.*, Ellwein v. United States, 778 F.2d 506, 509 (8th Cir. 1985).

44. *Compare* Rosenspan v. United States, 438 F.2d 905, 912 (2d Cir. 1971), *cert. denied*, 404 U.S. 864 (1971) (adopting a residential test of "home") *with* Weiberg v. Commissioner, 639 F.2d 434, 437 (8th Cir. 1981) (utilizing a vocational definition of "home").

45. *See infra* notes 46-68 and accompanying text.

46. *See, e.g.*, Commissioner v. Stidger, 386 U.S. 287, 293-95 (1967) (concluding that a Marine Corps captain's tax home was his military post in Iwakuni, Japan, even though he maintained a permanent home in California and acknowledging the vocational test, but making its conclusion based on the unique circumstances of military personnel); Peurifoy v. Commissioner, 358 U.S. 59, 59-61 (1958)

its part, the Service has consistently read *Flowers* as disallowing any commuting expense incurred from or to the employee's workplace.[47]

1. *Residential Home*

The less frequently utilized definition of "tax home" is that of the taxpayer's residential home.[48] Pursuant to the residential test, an employee's tax home is the employee's residence or abode.[49] The deductibility of travel expenses under the residential test hinges on whether the employee has traveled away from his or her home, as that word is generally understood.[50] Courts adopting the residential definition of home assert that "home" means home in its usual sense and not the employee's principal place of business.[51] While the Eighth Circuit initially adopted the residence test,[52] it now utilizes the vocational home definition.[53]

2. *Vocational Home*

The more frequently utilized definition of a tax home, and that advocated by the Service in most cases, is that of the taxpayer's vocational home.[54] Although the Supreme Court has declined to adopt any

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(declining to adopt a definition of tax home and instead determining that three construction workers who were respectively employed at a distant work site for periods of 20.5, 12.5, and 8.5 months, during which they maintained permanent residences elsewhere, were unable to deduct the amounts expended on transportation to the job site and board and lodging while at the job site); Commissioner v. Flowers, 326 U.S. 465, 472 (1946) (concluding that the Court did not need to determine what constituted the taxpayer's tax home because it could decide the case on other grounds).

47. *Flowers*, 326 U.S. at 474.

48. *Rosenspan*, 438 F.2d at 912.

49. *Id.* at 910-12.

50. *See, e.g.*, Six v. United States, 450 F.2d 66, 69 (2d Cir. 1971).

51. *See Rosenspan*, 438 F.2d at 910-11. The taxpayer in *Rosenspan* was a jewelry salesman who traveled during ten months of the year, but returned to a hotel in New York City five or six times each year. *Id.* at 907. The taxpayer attempted to use his employer's principal place of business as his "tax home" in order to deduct his travel expenses. *Id.* Although the court agreed that "home" meant home in the usual sense of the word, the court determined that the taxpayer had no such "home" and was thus not entitled to deduct his expenses. *Id.* at 912.

52. *See* Commissioner v. Janss, 260 F.2d 99, 104 (8th Cir. 1958) (concluding that although a college student was away from home, his travel to Alaska for summer employment was not done in the pursuit of his employer's business, and thus he was unable to deduct the costs of traveling to Alaska); Fischer v. Commissioner, 19 T.C.M. (CCH) 990 (1960); Schreiner v. McCrory, 186 F. Supp. 819, 823 (D. Neb. 1960) (permitting a traveling salesman to deduct travel expenses incurred while away from Omaha, Nebraska, where he maintained a residence with his wife).

53. Weiberg v. Commissioner, 639 F.2d 434, 437 (8th Cir. 1981).

54. *See* Hantzis v. Commissioner, 638 F.2d 248, 252-53 (1st Cir. 1981) (concluding that a Harvard law student residing in New York while employed as a summer associate was not entitled to deduct the cost of transportation, meals, and lodging incurred during her summer employment), *cert. denied*, 452 U.S. 962 (1981); Daly v. Commissioner, 662 F.2d 253, 254-55 (4th Cir. 1981) (concluding that a salesman was not permitted to deduct the costs of traveling from Virginia to Philadelphia, where the salesman's primary business was concentrated); Michel v. Commissioner, 629 F.2d 1071, 1074 (5th Cir. 1980) (using the vocational test in determining that the indefinite nature of the taxpayer's employment made Tehran, Iran, his tax home); Lewia v. Commissioner, 506 F.2d 1321, 1301 (D.C. Cir. 1974) (concluding that because a shoe factory consultant's distant work location had ceased being

definition of a "tax home,"[55] the Court has implicitly agreed with the vocational home definition, albeit in a split decision.[56] Under the vocational test, an employee's tax home is the employee's principal place of employment.[57] Deduction of travel expenses under the vocational test hinges on whether the employee has traveled away from the employee's principal place of business.[58] An employee's principal place of business is generally understood to be that work place location where the taxpayer has continued prospects of employment.[59]

The vocational test assumes that an employee *will* locate the employee's residence as close as possible to his or her workplace.[60] That assumption becomes complicated, however, when the employee cannot locate his or her residence near the workplace, such as where the employee's work-site is physically situated or restricted in such a way that the employee is literally precluded from living in close proximity to the work-site.[61] In such instances, the employee cannot satisfy the vocational test's presumption that the employee will maintain an abode near the employee's principal place of business because there is presumably no reasonable expectation that an employee will live where, in fact, the employee cannot live.[62] Despite the employee's inability to live near the

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temporary, it had become his tax home, and thus he was not permitted to deduct costs); Markey v. Commissioner, 490 F.2d 1249, 1253 (6th Cir. 1974); Rev. Rul. 75-432, 1975-2 C.B. 60; *see also* 26 C.F.R. § 1.911-2(b) (2001).

55. *See supra* note 46 and accompanying text.

56. *See* Commissioner v. Stidger, 386 U.S. 287, 290-92 (1967).

57. Rev. Rul. 73-529, 1973-2 C.B. 37.

58. *See Weiberg*, 639 F.2d at 437. Under the vocational test, a taxpayer's tax home is transient according to where the employee's principal place of business is located. Rev. Rul. 73-529, 1973-2 C.B. 37. A taxpayer who accepts permanent employment in a new location is deemed to have relocated his or her "tax home." *See, e.g.*, Jones v. Commissioner, 444 F.2d 508, 510-11 (5th Cir. 1971) (finding that a graduate student who relocated to Ohio from Texas to participate in his employer's fellowship program had relocated his tax home to Ohio and thus was not permitted to deduct costs of meals and lodging during the three-year school period).

59. *See* sources cited *supra* note 58.

60. *See* HB & R, Inc. v. United States, No. A1-96-141, slip op. at 4 (D. N.D. Apr. 29, 1998) (stating that "there is a 'reasonable expectation' that the taxpayer will locate his 'home' for tax purposes at his major post of duty so as to minimize the amount of business travel away from home that is required and that anything else is not business necessity but is a personal consideration"); *see also* Coombs v. Commissioner, 608 F.2d 1269, 1275 (9th Cir. 1979) (stating that the "tax home" is the taxpayer's personal residence when a regularly employed taxpayer maintains his or her personal residence within the general area of employment or as close as reasonably possible); Folkman v. United States, 615 F.2d 493, 495 (9th Cir. 1980) (stating that a taxpayer's tax home is "the . . . abode at his or her principal place of employment").

61. *See, e.g.*, United States v. Taufemer, 407 F.2d 243, 246-47 (10th Cir. 1969) (denying the deduction of the costs associated with commuting twenty-seven miles from a rocket testing facility to the nearest housing even though the employee was not permitted to reside at the facility and could not find housing in the community nearest the facility).

62. *See HB & R*, No. A1-96-141, slip op. at 4. In the opinion of the district court in *HB & R*, "it is wrong to attempt to apply general principles which work 99 percent of the time to the 1 percent where those regulations do not fit." *Id.*

work-site, however, courts in such cases have refused to permit deduction of the employee's expenses incurred in traveling to work.[63]

Thus, in *Edmands v. Commissioner*,[64] the Tax Court refused to permit an oil worker to deduct the costs of traveling from his home to his place of employment at a pump station on the Trans-Alaska pipeline, where he was unable to live.[65] The oil worker worked eight days at the pump station, followed by six days of rest at his home in Kasilof, Alaska.[66] Every six days the taxpayer drove twenty-two miles from Kasilof to Kenai, Alaska, to take a commercial airline flight to Anchorage, Alaska, where he caught a charter flight directly to the pump-station.[67] Precluding the taxpayer from deducting the costs of the commercial flight from Kenai to Anchorage, the Tax Court concluded that the costs constituted personal commuting expenses.[68]

E. TRAVEL EXPENSES AND THE EMPLOYER

The complexities of the employee's deduction of travel expenses is further complicated when an employer reimburses the employee or otherwise pays for the expenses.[69] Generally, an employer may reimburse an employee for ordinary and necessary business expenses, such as those incurred when an employee travels from one work location to another.[70] In such instances, the employer may reimburse the employee and deduct the expenses from its taxable income, so long as the expenses are substantiated and the reimbursement payment is made separately

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63. *Tauferner*, 407 F.2d at 247; Pilcher v. Commissioner, 651 F.2d 717, 718 (10th Cir. 1981) (precluding deduction of the costs of commuting sixty-seven miles to an employee's work-site); Coombs v. Commissioner, 608 F.2d 1269, 1276 (9th Cir. 1979) (precluding deduction for the costs of commuting sixty-five miles from nuclear test site to nearest habitable community); Sanders v. Commissioner, 439 F.2d 297 (9th Cir. 1971) (precluding a civilian employee of an air force base to deduct the costs of commuting there, even though he was prohibited from living on the base). *But see* Wright v. Hartsell, 305 F.2d 221, 225 (4th Cir. 1962) (concluding that "a taxpayer's inability to live near his job site is a valid ground for deduction as travel expense of the resulting cost of his transportation, food and lodging").

64. 58 T.C.M. (CCH) 167 (1989).

65. *Edmands*, 58 T.C.M. (CCH) at 167.

66. *Id.*

67. *Id.*

68. *Id.* Interestingly, the Service did not seek to include as income the value of the employer provided airfare from Anchorage to the pump station. *Id.* This is surprising, given the Service's previous success in arguing against deduction of expenses paid in traveling to work sites where employees were not permitted to live. *See supra* notes 61-63 and accompanying text. The court did not discuss the deductibility of the twenty-two mile driving commute from Kasilof to Kenai. *Edmands*, 58 T.C.M. (CCH) at 167.

69. 26 C.F.R. § 31.3121(a)-1(h) (2001).

70. *Id.* (applicable to tax periods before July 1, 1990); *Id.* §§ 31.3401(a)-4(d), 31.3121(a)-3(c) (applicable to tax periods after June 30, 1990).

from the employee's wage payment.[71] When this is done, the reimbursement typically does not constitute either taxable income or a wage to the employee.[72]

In Revenue Ruling 76-453, however, the Service asserted that reimbursements paid to employees for commuting expenses would be considered wages for purposes of FICA and income tax withholding.[73] Congress immediately responded by issuing a moratorium against the position advanced by the ruling.[74] Indeed, prior to the issuance of Revenue Ruling 76-453, several courts had rejected the Service's arguments that an employer's reimbursement or payment of employee travel expenses constituted wages subject to withholding.[75]

F. THE NARROW VIEW OF AN EMPLOYER'S WITHHOLDING OBLIGATION

As noted earlier, "wages" is a significantly narrower concept than "gross income" because while wages invariably constitute income to an employee, not all income is composed of wages.[76] A circumscribed

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71. *Id.* §§ 31.3401(a)-4(a), 31.3121(a)-3(a).

72. *Id.* §§ 31.3401(a)-4(a), 31.3121(a)-3(a).

73. Rev. Rul. 76-453, 1976-2 C.B. 86. Rev. Rul. 76-453 revoked former Rev. Rul. 53-190 and was issued in response to the Tax Court's decision in *Turner v. Commissioner*, 56 T.C. 27 (1971). In *Turner*, the Tax Court determined that "commuting is commuting," whether to a temporary or permanent work-site; consequently, the costs associated with such commutes are non-deductible, and employer reimbursements of those costs should be included in the wage base for employment tax purposes. *Id.*

74. *See* Act of October 7, 1978, Pub. L. 95-427, sec. 2, 92 Stat. 966 (codified in scattered sections of 26 U.S.C.) (mandating that Rev. Rul. 76-453 not be applied to taxable periods between January 1, 1977 and December 31, 1979); Tax Treatment Extension Acts of 1977, Pub. L. 95-615, sec. 2, 92 Stat. 3097 (codified in scattered sections of 26 U.S.C.); Act of December 29, 1979, Pub. L. 96-167, sec. 2, 93 Stat. 1275 (codified at 26 U.S.C. § 62 (1994 & Supp. V)) (mandating that the moratorium be extended to May 31, 1981); *see also* Prop. Treas. Reg. § 1.61-16, 40 Fed. Reg. 41 (1975) (setting forth a proposed regulation concerning taxation of fringe benefits). In response to the moratorium, the Service announced that the effective date of Rev. Rul. 76-453 would be "suspended indefinitely" pending the issuance of proposed regulations inviting public comment. Rev. Rul. 76-453, 1977-2 I.R.B. 45. The Service also advised examining agents not to make adjustments for substantiated transportation expenses to temporary job sites. *See* Michael D. Rose, *The Deductibility of Daily Transportation Expenses To and From Distant Temporary Work Sites*, 36 VAND. L. REV. 541, 543 (1983). Congress finally addressed the issue in the Deficit Reduction Act of 1984, Pub. L. 98-369, 98 Stat. 494, by including "fringe benefits" as an item of gross income in I.R.C. § 61(a)(1). *See generally*, Peter W. Colby, Comment, *Federal Withholding on Employee Fringe Benefits for Income and Social Security Taxes*, 70 CAL. L. REV. 178 (1982); David M. Graf, *Taxation of Fringe Benefits*, 27 S. TEX. L. REV. 251 (1986).

75. *See* Stubbs, Overberg & Assoc., Inc. v. United States, 445 F.2d 1142, 1148 (5th Cir. 1971) (finding that a per diem paid to employees for trips from Houston, Texas, to Bartlesville, Oklahoma, to perform a contract that lasted one year was not wages subject to withholding); Peoples Life Ins. Co. v. United States, 373 F.2d 924, 935 (Ct. Cl. 1967) (holding that travel expenses paid to employees to attend a convention did not constitute wages subject to withholding); Acacia Mutual Life Ins. v. United States, 272 F. Supp. 188, 189 (D. Md. 1967); England v. United States, 345 F.2d 414, 417 (7th Cir. 1965), *cert. denied*, 382 U.S. 986 (1966).

76. *See supra* Part I.B.

interpretation of what constitutes wages subject to withholding is consistent with the policy of minimizing an employer's exposure to liability for withholding another taxpayer's, such as its employee's, taxes.

Thus, in *Central Illinois Public Service Co. v. United States*[77] the Supreme Court articulated its narrow view of the withholding statutes.[78] The employer in *Central Illinois* reimbursed its employees for lunch on occasions when they were not away on business overnight, but were nevertheless completing business-related duties.[79] Rejecting the Service's attempt to subject the reimbursements to withholding taxes, the Supreme Court stated:

> [I]t is one thing to say that reimbursements constitute income to the employees for income tax purposes, and it is quite another thing to say that it follows therefrom that the reimbursements in 1963 were subject to withholding. There is a gap between the premise and the conclusion and it is a wide one. . . . To require the employee to carry the risk of his own tax liability is not the same as to require the employer to carry the risk of the tax liability of its employee. Required withholding, therefore, is rightly much narrower than subjectability to income taxation.[80]

Since its decision in *Central Illinois*, the Supreme Court has continued to subscribe to a limited view of an employer's withholding obligation.[81] Thus, in *Rowan Cos., Inc. v. United States*,[82] the Supreme Court concluded that an employer did not have a duty to withhold FICA and income taxes on the value of lodging and meals provided to its employees on an offshore oil rig.[83] Although the employees in *Rowan* were flown at company expense up to sixty miles from land to the offshore oilrig, the Service argued only for taxation of the value of the food and lodging.[84] Noting that "'wages' is a narrower concept than

77. 435 U.S. 21 (1978).
78. *Central Illinois*, 435 U.S. at 21.
79. *Id.*
80. *Id.* at 29.
81. *Id.*
82. 452 U.S. 247 (1981).
83. *Rowan*, 452 U.S. at 254.
84. *Id.*

'income,'"[85] the Court concluded that the value of employer provided meals and lodging was not wages subject to FICA withholding.[86]

II. THE EXIGENCIES OF HB & R, INC.'S BUSINESS

In November 2000, the Eighth Circuit was called upon to resolve whether the value of employer-paid airline tickets was wages subject to FICA and income tax withholding.[87] The taxpayer at issue in *HB & R, Inc. v. United States*,[88] was HB & R, Inc. (HB & R), a Montana corporation with its principal place of business in Dickinson, North Dakota.[89] HB & R provides "hot oil services"[90] to oil companies at Prudhoe Bay in Alaska, also known as the "North Slope."[91] The services are provided on an as-requested basis, with the oil companies dictating the necessity and amount of work to be done.[92]

Because of the inhospitable climate and security concerns, it is impossible to live on the North Slope.[93] The nearest residential community is Fairbanks, Alaska, nearly 500 miles away by a gravel road, on which no one is permitted to drive without permission of the oil

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85. *Id.* Although the Social Security Amendments of 1983 statutorily overruled *Rowan*, at least two circuit courts have relied on *Rowan* to hold that amounts excluded from income are not wages subject to FICA withholding. *See* Pub. L. No. 98-21, 97 Stat. 65, 127 (1983) (overruling *Rowan*); *see also* Dotson v. United States, 87 F.3d 682, 689 (5th Cir. 1996) *and* Gerbec v. United States, 164 F.3d 1015, 1025 (5th Cir. 1999) (relying on *Rowan*).

86. *Rowan*, 452 U.S. at 254; *see also* I.R.C. § 3121(a) (specifying that nothing in the regulations concerning income tax withholding, "which provides an exclusion from 'wages' . . . shall be construed to require a similar exclusion from 'wages' in the regulations prescribed for purposes of [FICA withholding]"; *S. Rep. No. 98-23, at 42 (1983), reprinted in* 1983 U.S.C.C.A.N. 143, 183 (providing that "amounts exempt from income tax withholding should not be exempt from FICA unless Congress provides an explicit FICA tax exclusion"); Anderson v. United States, 16 Cl. Ct. 530, 536 (1991) (holding that the language in § 3121 evidences the "manifest congressional intent that merely because an item is exempt from federal income taxes does not mandate that it be exempt from FICA taxes").

87. *HB & R, Inc. v. United States, 229 F.3d 688, 689 (8th Cir. 2000).*

88. 229 F.3d 688 (8th Cir. 2000).

89. *HB & R*, 229 F.3d at 689.

90. The hot oil services consist primarily of the injection of fluid under high pressure into oil wells to inhibit the formation of scale in the pipes, to control the formation of paraffin in the oil being pumped, to heat flow lines from the well to the pipeline, and to introduce heated methanol into the well to control permafrost. Brief on Appeal for Appellant and Cross-Appellee at 3, HB & R, Inc. v. United States, 229 F.3d 688 (8th Cir. 2000) (No. 99-3206) [hereinafter "Appellant's Brief on Appeal"].

91. *HB & R*, 229 F.3d at 689. The oil companies with which HB & R contracted during the tax years in question were British Petroleum, Arco Petroleum, and Conoco. Appellant's Brief on Appeal at 3, *HB & R* (No. 99-3206).

92. Appellant's Brief on Appeal at 3-4, *HB & R* (No. 99-3206). HB & R is paid on a job-by-job basis. *Id.* at 4. Consequently, if no work is done, HB & R is not paid. *Id.* Likewise, if there are no jobs to be done, HB & R's employees do not work and are not paid. *Id.* at 9.

93. *HB & R*, 229 F.3d at 689. "Life, with a family, is not possible at the work site." HB & R, Inc. v. United States, No. A1-96-141, slip op. at 2 (D. N.D. Apr. 28, 1998). Access to the entire 80 to 100 square-mile area known as the North Slope is denied without a special permit issued by the oil companies. *See* Appellant's Brief on Appeal at 6, *HB & R* (No. 99-3206). There is no land for sale and no apartments or other rental facilities in the area. *Id.* There are no medical facilities except for a first-aid station manned by a paramedic. *Id.*

companies.[94] Because of these circumstances, when HB & R receives a work request from an oil company, it deploys its workers from their homes to the North Slope for a three-week on and three-week off rotation.[95] During the three-week work rotation, the employees live in oil company-owned barracks where they enjoy "virtually no recreational amenities."[96] The workers can be called upon to work anywhere within the one hundred square mile region of the North Slope and often work very long hours.[97]

Most of HB & R's employees live in the continental United States (the "lower forty-eight").[98] Consequently, when it is an employee's turn to travel to the North Slope, the employee must leave his or her home in the lower forty-eight and fly to the North Slope, stopping first in Anchorage, Alaska, and then flying on to the Dead Horse Airport.[99] Although HB & R has offered its employees a $400 per month salary incentive to relocate to Alaska, most employees continue to live in the lower forty-eight.[100] HB & R's efforts to recruit Alaska natives for employment have also been largely unsuccessful.[101]

To transport its workers to the North Slope, HB & R has uniformly purchased commercial airline tickets for its employees, which cost, on average, between $1,000 and $1,200 per round-trip ticket from each employee's home to the Dead Horse Airport.[102] HB & R deducts the

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94. Appellant's Brief on Appeal at 6-7, *HB & R* (No. 99-3206).

95. *HB & R*, 229 F.3d at 689. Every employee has an alternate who works during the alternate three-week period. Appellant's Brief on Appeal at 5, *HB & R* (No. 99-3206). During the three-week "off" period, the workers can be called upon to perform services for HB & R in the lower forty-eight states. *Id.* at 8.

96. *HB & R*, 229 F.3d at 689; *see also* Appellant's Brief on Appeal at 5, *HB & R* (No. 99-3206). The rooms are approximately eight feet by twelve feet in size and house bunk beds for the workers. *Id.* There are typically two to four workers per room. *Id.* The oil companies own the barracks and rent the space to HB & R for seventy-five dollars per day per worker. *Id.* Meals are served cafeteria-style twenty-four hours per day, and the workers are not permitted to have alcohol. *Id.* The toilet and shower facilities are communal or military-style. *Id.* Firearms are prohibited, and the workers cannot fish or hunt. *Id.* at 5-6. There is no entertainment, such as movies, gyms, restaurants, swimming pools, or other recreation facilities provided for the workers. *Id.* at 5.

97. Appellant's Brief on Appeal at 7, *HB & R* (No. 99-3206). Because of the weather and varying demands of the oil companies, the precise amount of work to be done at any time is nearly impossible to predict. *Id.* During the past twenty years, the number of workers on the North Slope has varied between nine and twenty. *Id.* No work is performed during "white-out" periods when the visibility is low due to snowstorms or when the temperature outside is less than forty degrees below zero Fahrenheit. Brief on Appeal for Appellee and Cross-Appellant at 5, *HB & R, Inc. v. United States*, 229 F.3d 688 (8th Cir. 2000) (No. 99-3206) [hereinafter "Appellee's Brief on Appeal"].

98. *HB & R*, 229 F.3d at 689.

99. *Id.*

100. *Id.*

101. HB & R v. United States, No. A1-96-141, slip op. at 2 (D. N.D. Apr. 28, 1998). However, HB & R never posted job listings anywhere in Alaska, choosing instead to advertise by "word of mouth." Appellee's Brief on Appeal at 6, *HB & R* (No. 99-3206).

102. *HB & R*, 229 F.3d at 689. As a practical matter, most of HB & R's employees would be unable to independently purchase these tickets because of the high cost and the frequency with which

costs of the tickets as an ordinary and necessary business expense under Internal Revenue Code § 162, but does not include the value of the tickets in its employees' wages.[103]

For the tax years 1991, 1992, and 1993, the Service assessed tax deficiencies on HB & R because the company did not withhold or pay income tax or FICA taxes on the value of the employee airfare to the North Slope.[104] After duly paying the assessed deficiencies and having its administrative claim for refund denied by the Service, HB & R filed a refund action in the United States District Court for the District of North Dakota.[105] On appeal from the district court's decision, the Eighth Circuit held that the value of the airline tickets paid for by HB & R was not wages subject to either income tax or FICA tax withholding .[106]

III. THE EXIGENCIES IN ACTION

The crux of *HB & R* was whether the value of employer-paid airfare to the workplace constituted wages subject to income and FICA taxes.[107] The government argued that because the cost of commuting to one's workplace is a non-deductible expense, HB & R's payment of the cost of travel to the North Slope work-site constituted remuneration to its employees and that this remuneration was wages subject to both FICA and income taxes.[108] According to the government's theory, if HB &

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the tickets must be purchased. Appellant's Brief on Appeal at 9, *HB & R* (No. 99-3206).

103. Appellant's Brief on Appeal at 9, *HB & R* (No. 99-3206). The pay for a North Slope employee is about $18 per hour, with the opportunity for significant overtime. *Id.* Including overtime pay, the average North Slope worker earns $40,000 per year for twenty-six weeks of work. *Id.* Including both benefits and salary, the average cost to HB & R for each employee is approximately $120,000 per year. *Id.*

104. *HB & R*, 229 F.3d at 689. The Service assessed HB & R $183,129 in taxes, $97,617.31 in interest, and a penalty of $53.91, for all four quarters of 1990 and 1991 and the first three quarters of 1992. Appellee's Brief on Appeal at 2, *HB & R* (No. 99-3206).

105. *HB & R*, 229 F.3d at 689. HB & R paid the Service $722.77 for the third quarter of 1992 and promptly filed its administrative refund claim. Appellee's Brief on Appeal at 1-2, *HB & R* (No. 99-3206).

106. *HB & R*, 229 F.3d at 692. The United States District Court for the District of North Dakota came to a divergent result, from which both the Service and HB & R appealed. HB & R v. United States, No. A1-96-141, slip op. at 5-6 (D. N.D. Apr. 29, 1998). Judge Patrick A. Conmy determined that the airfare from the lower forty-eight to Anchorage constituted wages because Anchorage was the closest location to which the employees could reasonably be expected to relocate. *Id.* The district court explained, however, that

> [t]he unique factual situation presented here when viewed in conjunction with the incredible prolixity and complexity of the tax code and the regulations promulgated in connection with that code operate, in the opinion of the court, to exonerate the employer from liability for failure to withhold.

Id. at 5 (citing Cent. Ill. Pub. Serv. Co. v. United States, 435 U.S. 21, 31-32 (1978)). Then, inexplicably, the court granted the Service's motion for summary judgment on the issue of failure to withhold FICA taxes and granted HB & R's motion for summary judgment on the issue of failure to withhold income taxes. *Id.* at 5-6. As a result, HB & R was excused from withholding income taxes, but not FICA taxes. *Id.*

107. *HB & R*, 229 F.3d at 690-91.

108. *Id.* at 690. Because Anchorage is the city nearest Dead Horse where HB & R's employees

R's employees had paid for the airfare themselves, they could not have deducted the airfare as a travel expense under § 162(a)(2) because, under the vocational test, the North Slope was the employees' tax home.[109] As such, the reimbursement or payment of any such expenses could not be excluded from the wage base subject to withholding under §§ 3121 or 3401.[110]

Conversely, HB & R argued that because the airfare costs were incurred by HB & R as a result of the exigencies of its business, the costs did not constitute commuting expenses.[111] HB & R further asserted that because the travel costs were not otherwise non-deductible commuting expenses they were not remuneration or wages subject to income or FICA withholding.[112] Claiming that the ban on deducting "commuting" expenses applies only when the expenses are incurred on a daily basis, HB & R also argued that because of the intermittent nature of its employees' travel, the airfare did not constitute non-deductible commuting expenses.[113]

A. THE COURT REJECTS THE GOVERNMENT'S SYLLOGISM

In formulating its holding, the Eighth Circuit first noted the general rule that "an employee's expenses in commuting from home to work are personal, not deductible business expenses."[114] Discounting the Service's "syllogism" that because commuting expenses are non-deductible expenses for the employee, HB & R's payment of such expenses constituted taxable wages subject to withholding, the court articulated a narrow view of the employer's obligation to withhold.[115] Quoting *Central Illinois*, the court noted that while reimbursement of certain expenses may constitute taxable income to the employee, it does not necessarily follow that the employer has a withholding obligation.[116]

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could reasonably be expected to reside, the Service did not assert that the costs of airfare from Anchorage to Dead Horse should be considered wages. Appellee's Brief on Appeal at 12, 20, *HB & R* (No. 99-3206). This is surprising in light of the Service's previous success in precluding the deduction of commuting expenses to work-sites where the employee was unable, for one reason or another, to live in close proximity to the work-site. *See supra* notes 59-61, and accompanying text.

109. Appellee's Brief on Appeal at 21, *HB & R* (No. 99-3206).

110. *Id.* In its opinion, the district court noted that the Service's argument "is stated in a wonderfully pellucid manner in the filings, is logical, supported by numerous decisions and in the opinion of the Court, wrong." HB & R v. United States, No. A1-96-141, slip op. at 2 (Apr. 28, 1998).

111. Appellant's Brief on Appeal at 14, *HB & R* (No. 99-3206).

112. *Id.*

113. *Id.* 13-22.

114. HB & R v. United States, 229 F.3d 688, 690 (8th Cir. 2000).

115. *Id.* Rejecting the IRS's argument at the district court level, Judge Conmy aptly noted that

> the IRS was wrong in attempting to impose liability on the total sum expended for airline travel despite the ridiculous outcome which results from such a holding. Alice appears to be alive and well not only in wonderland, but also in the attempt of the IRS to make reality subordinate to its rules.

HB & R v. Commissioner, No. A1-96-141, slip op. at 5 (Apr. 28, 1998).

116. *HB & R*, 229 F.3d at 690.

Indeed, "[r]equired withholding, therefore, is rightly much narrower than subjectability to income taxation."[117]

The court then considered the Treasury Regulations relevant to the withholding statutes and specifically looked to Treasury Regulation sections 31.3401(a)-1(b) and 31.3121(a)-1(h).[118] Those Regulations provide:

> *Traveling and other expenses.* Amounts paid specifically—either as advances or reimbursements—for traveling or other bona fide ordinary and necessary expenses incurred or reasonably expected to be incurred in the business of the employer are not wages and are not subject to withholding.[119]

Relying on the unambiguous language of the Regulations, the court determined that they "do not expressly distinguish between commuting from home to work, and other employee traveling, so long as the expense is ordinary and necessary to the business of the employer."[120] The court stated that when viewed from the perspective of the employer HB & R, the costs associated with transporting workers to the North Slope were incurred regularly and necessarily in the business of providing hot oil services to North Slope oil producers.[121] Because the withholding regulations instruct the employer to exclude from withholding those expenses incurred regularly and necessarily in the pursuit of *its* business, as opposed to the employee's, the court concluded that HB & R was justified in not withholding income and FICA taxes based on the value of the airfare.[122]

B. THE COURT DOES NOT ENGAGE IN A TRADITIONAL ANALYSIS

By relying on the Treasury Regulations applicable to withholding of income and FICA taxes, the Eighth Circuit artfully avoided employing a traditional travel expense analysis.[123] Pursuant to *Flowers* and its progeny, the Eighth Circuit is bound to ensure that travel expenses are deducted under § 162 only when they are reasonable and necessary,

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117. *Id.* at 690-91 (quoting Cent. Ill. Pub. Serv. Co. v. United States, 435 U.S. 21, 29 (1978)).

118. *Id.* at 691.

119. 26 C.F.R. § 31.3401(a)-1(b) (2001) (excluding travel expenses from wages subject to income tax withholding); 26 C.F.R. § 31.3121(a)-1(h) (2001) (excluding travel expenses from wages subject to FICA tax withholding).

120. *HB & R*, 229 F.3d at 691.

121. *Id.* The court went so far as to say that the regulations "instruct the employer to focus on whether travel expenses are ordinary and necessary to *its* business." *Id.*

122. *Id.*

123. *Id.* (distinguishing *Flowers* because in that case the Court "view[ed] the expenses from the income tax perspective of the employee, rather than the withholding tax perspective of the employer").

incurred while away from home, and incurred in the pursuit of business.[124] Pursuant to Code §§ 3101(a) and 3401(a), the deductibility of employee travel expenses under § 162 is linked to exclusion from wages for withholding tax purposes because travel expenses which could be deducted by the employee under § 162 are necessarily excluded from the realm of wages subject to withholding.[125]

The court in *HB & R*, however, did not employ such an analysis.[126] Presumably, the court would have determined that the airfare to the North Slope was reasonable and necessary (prong one) because flying the workers to the North Slope was the only means of supplying HB & R with a workforce at the site. Furthermore, the court expressly concluded that the airfare was incurred regularly and necessarily in the pursuit of HB & R's business (prong three).[127] Thus, as in many other cases, deductibility of the airfare would have hinged on prong two of the *Flowers* test; namely, whether HB & R's employees were away from "home" when the expenses were incurred.[128]

Given the Eighth Circuit's prior adoption of the vocational test, the HB & R employees would have presumably been expected to, at least, reside in Anchorage, thus making Anchorage their "tax home." Consequently, the airfare from the lower forty-eight states to Alaska would not have been incurred while away from home. Instead, the airfare would have constituted normal commuting expenses, the payment of which by HB & R would have been the payment of wages subject to withholding.

Thus, had the court simply employed a traditional travel expense analysis, it is likely that the airfare would have been considered a non-deductible commuting expense and thus includible in wages subject to withholding. HB & R's benefit from the court's alternative analysis only underscores the necessity that the Supreme Court determine the "tax home" issue once and for all.

C. THE COURT PASSES ON THE ISSUE OF INCLUSION IN GROSS INCOME

Although not directly addressing the issue, the court's decision did not preclude assessment of deficiencies on the individual oil workers employed by HB & R. Indeed, the district court noted that if the Service "has the desire to pursue the individual employees who are responsible for the payment of taxes on under reported income due to the 'personal

124. Commissioner v. Flowers, 326 U.S. 465, 470 (1946).
125. *HB & R*, 229 F.3d at 690-91.
126. *Id.* at 691.
127. *Id.*
128. *Flowers*, 326 U.S. at 470.

nature' of the air fares, then the court wishes them [the Service] well."[129] So, while the court determined that the value of the airfare did not constitute "wages" subject to withholding, it bypassed the issue of whether the individual employees were required to include that value in their income.[130]

IV. IMPLICATIONS OF THE EIGHTH CIRCUIT'S DECISION

While the facts of HB & R seem peculiar to exigencies of HB & R's business, workers on the North Slope of Alaska are not the only employees who reside in one location and must travel to distant work locations for some period of time. For example, most members of Congress maintaining a residence in their home state are unable to simply drive from that residence to Washington, D.C., each day of a legislative session. In recognition of the special circumstances faced by Congressional members, the Tax Reform Act of 1976 established a special travel expense deduction rule for the members.[131] The Act permits members of Congress to elect to be "away from home" and "in pursuit of trade or business" each legislative day as an exception to § 162.[132] Similarly, a special exception was carved out for federal employees participating in federal criminal investigations.[133]

Commercial fisherpersons who board their ships at a home port and travel far out to sea to reach remote fishing grounds where they fish for multiple weeks before returning to port with their catch are another example.[134] Under such circumstances, it is impossible for the fisherpersons to relocate their residential home to the situs of their trade on the ship at sea.[135] In such instances, the fisherpersons "tax home" is considered their homeport where they ordinarily begin and end their trips.[136] The fisherpersons may deduct travel and living costs only when away for a period longer than an ordinary workday and overnight.[137]

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129. HB & R v. United States, No. A1-96-141, slip op. at 5 (D. N.D. Apr. 28, 1998).

130. *Id.* at 5-6. Presumably, however, the deficiency assessment period for most of the individual taxpayer employees had already expired by the time the Eighth Circuit's decision was issued. *HB & R*, 229 F.3d at 692.

131. Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520 (codified at 26 U.S.C. § 162(h) (1994 & Supp. V 1999)).

132. 26 U.S.C. § 162(h). Prior to Congress' codification for its members' travel expenses, members of Congress were not permitted to deduct expenses incurred in Washington, D.C. Lindsay v. Commissioner, 34 B.T.A. 840 (1936).

133. IRS Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 818, (codified at 26 U.S.C. § 162(h)(4)).

134. Rev. Rul. 55-235, 1955-1 C.B. 274.

135. *Id.*

136. *Id.*

137. *Id.*

As these examples illustrate, the exigencies of HB & R's business are not, in fact, entirely unique and need to be treated in a rational fashion although the circumstances may seem outside the norm. Indeed, taken to its extreme, the Service's position could require future workers on space stations to pay FICA and income taxes based on the value of transporting the workers, via rocket, to their space stations.

Ultimately, the Eighth Circuit made the correct decision. Pursuant to Treasury Regulation sections 31.3401(a)-1(b) and 31.3121(a)-1(h), the court properly shifted the focus from the employee to the exigencies of the employer's business.[138] Where the nature of the employer's business is such that it necessarily must pay travel expenses on behalf of its employees, those expenses are not and should not be considered wages subject to withholding.[139]

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138. 26 C.F.R. § 31.3401(a)-1(b) (2001); 26 C.F.R. § 31.3121(a)-1(h) (2001).
139. HB & R v. United States, 229 F.3d 688, 692 (8th Cir. 2000).

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